

# EXHIBIT

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## Venture firms' `creative destruction'

By Matt Marshall  
Mercury News

There's been some shakin' in the secretive world of Silicon Valley venture capital, and it could be part of a larger industry transformation.

The change includes too much money trying to coagulate at a couple of dozen of the best firms, and a realization that Silicon Valley may no longer be the most profitable place to build small companies into bigger ones.

Last week, a band of four venture capitalists bolted from Lightspeed Venture Partners, one of those venerable major firms nestled along ground zero for venture capital, Sand Hill Road.

Lightspeed is a 34-year-old venture firm, but hasn't done that well recently. Lightspeed's \$800 million fund, raised in 2000, shows an internal rate of return of -17.2 percent, according to data published by investor California Public Employees' Retirement System. That's slightly lower than the average -13.3 percent, reported by Venture Economics.

### Darwinian shakeout

The majority of venture firms don't do that well. The bottom half generally don't make any money at all. So most investors try to put their money with the top 25 percent of performing funds. And if they don't get into those, many investors don't play at all.

A Darwinian shakeout unfolds: Underperforming venture firms fizzle out of existence; newer, hungrier firms take their place.

So what's going on at Lightspeed? The firm said little, other than confirm partners Gill Cogan and Carl Showalter, with an unspecified ``team" of others, will raise a separate fund.

Lightspeed's remaining partners will continue on their own. Personnel changes ``are not necessarily a negative development," says David Cowan, a partner at Bessemer Venture Partners, a firm that doesn't raise money from outside investors.

All of these things may be specific to Lightspeed, but they may also be part of the larger picture.

Take, for example, developments at big-name fund Mayfield, which surfaced Friday, the day after the Lightspeed defection.

### The Mayfield story

A leading trade publication, Private Equity Week, reported that Mayfield had lost seven respected institutional investors while raising its latest fund, in part because it had allegedly demanded more of the profits it generated from earlier funds than some investors believed they'd agreed to. Mayfield, which backed SGI, Compaq and Genentech, among others, declined comment.

But it also emerged that Mayfield was generating so much interest for investors that it could get away with it -- at least short-term. And this, even though its recent funds haven't been doing that well. Fact is, brand-name venture firms can continue to ride on their reputation for a while.

This is where the view of Peter Rip is worth considering.

Rip is a managing director at Leapfrog Ventures, a smaller fund that focuses on nurturing early-stage start-ups with small amounts of capital.

Until the 1990s, venture capital investing in places like Boston and Silicon Valley was a breeze. Precious little capital was available for very few promising start-ups. The select few VCs with access could keep hitting grand slams with companies like Cisco, Sun and Intel.

## Seeking the best

But since 2000, international investors are still seeking to place hundreds of billions of dollars with the best Silicon Valley firms, explains Rip. Even after the bubble burst, Menlo Park's venture firms have been considered the best around. Many people agree.

Rip's analogy is New York, which became a banking center. Its money circulates globally, but much of it is not having any impact on New York itself. The same thing is happening with expensive Silicon Valley.

Now bloated, firms are seeking to put hoards of dollars to work, and are being forced to invest in larger, later-stage companies, which require bigger amounts of capital. Some of those companies will be in Silicon Valley, but many more may be in China and other cheaper places. Job growth here will decline.

``These forces are causing the industry to retool," Rip says, calling it ``creative destruction."

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